IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

I TE KŌTI MATUA O AOTEAROA
TĀMAKI MAKAURAU ROHE

CIV-2018-404-1727
[2019] NZHC 1105

UNDER	the Companies Act 1993 and Part 19 of the High Court Rules
BETWEEN	KENNETH PETER BROWN and PAUL THOMAS MANNING Applicants
AND	HEARTLAND BANK LIMITED Respondent

Hearing:	13 November 2018
Appearances:	P J Crombie for the Applicants K M Wakelin for the Respondent
Judgment:	21 May 2019

INTERIM JUDGMENT OF ASSOCIATE JUDGE SMITH

This judgment was delivered by me on 21 May 2019 at 10.30am, pursuant to r 11.5 of the High Court Rules

Registrar/Deputy Registrar

Solicitors / Counsel:
CooneyLeesMorgan, Tauranga
Grove Darlow, Auckland

[1] The applicants (the liquidators) apply for directions under s 284 of the Companies Act 1993 (the Act).

[2] The case relates to a company called Stages Civil & Electrical Ltd (In Liquidation) (Stages), which went into liquidation in September 2015. The liquidators originally appointed were Mr Brown and Mr Paul Clark, an associate of Mr Brown at the accounting firm BDO. Mr Clark retired as liquidator in 2017, and Mr Manning was appointed co-liquidator of Stages on 7 July 2017.

[3] The liquidators are holding a fund of $120,486.14 in the liquidation of Stages (the Fund), which is substantially comprised of the realisation of trade debts owed to Stages. The liquidators believe that the Fund should be shared between Stages' preferential creditors (the Commissioner of Inland Revenue and former employees of Stages), and they apply for directions accordingly.

[4] The respondent (Heartland) had entered a factoring agreement with Stages, under which it acquired all of Stages' current and future accounts receivable in exchange for cash payments made to Stages from time to time. It contends either that it owns the Fund, or that certain securities taken by it over Stages' accounts receivable entitle it to the Fund in priority to the preferential creditors.

Background

[5] Stages was in the business of laying fibre optic cable for ultrafast broadband. Its sole source of revenue was from a subcontract it had with a company called Broadspectrum (New Zealand) Ltd, previously known as Transfield Services (New Zealand) Ltd. I will refer to this company as "Broadspectrum". Broadspectrum was the head contractor under a contract with Telecom New Zealand Ltd.

[6] In 2017 Stages got into financial difficulty as a result of late payment of its invoices by Broadspectrum, and it could not pay its staff. Stages' shareholders appointed Mr Brown and Mr Clark as liquidators on 16 September 2015.

The assets that make up the Fund

[7] At the date of the liquidation, Stages had issued the following invoices to Broadspectrum that were unpaid:

Invoice No.	Date	Amount
666	30 June 2015	$50,443.42
675	31 August 2015	$17,713.89
676	31 August 2015	$120,025.72

[8] In addition to those unpaid invoices, the liquidators calculated that there was substantial unbilled work in progress on Stages' subcontract with Broadspectrum as at the liquidation date. They issued an invoice for $105,372.20 for the unbilled work in progress, on 25 November 2016.

[9] The total of the four invoices, including the post-liquidation invoice, came to $293,555.23. However, Broadspectrum had claims of its own against Stages, in respect of allegedly defective work carried out on the subcontract. Broadspectrum's claims included "strike claims", where Stages had allegedly damaged pipes or other infrastructure when digging trenches to lay the fibre optic cable.

[10] The liquidators considered Broadspectrum's claims, and concluded that, in order to achieve a settlement, they would credit the sum of $177,024.94 to Broadspectrum by way of set-off against the $293,555.23 claimed by Stages. They proposed settlement in the sum of $116,530.29.

[11] On 1 November 2016 Broadspectrum accepted the settlement at $116,530.29, and on 25 November 2016 it paid the sum of $103,168.96 (including GST) to the liquidators. After accounting to the Inland Revenue department for the GST component of that sum, the net amount received by the liquidators was $89,712.14. The liquidators say that Broadspectrum has failed or refused to pay the balance of the agreed settlement amount.

[12] The net figure of $89,712.14 paid by Broadspectrum is the first and most substantial component of the Fund. There are two other components. First, the liquidators have received a payment of $10,774 arising from an insurance claim in

respect of a claim made against Stages by Broadspectrum. Among the claims made by Broadspectrum following the liquidation was a claim for a sum of $36,549.27 relating to damaged cables at Pohutukawa Drive, Hamilton. An insurance claim was submitted pre-liquidation, which included reasons why Stages should not be held liable. The insurers determined that Stages was 50 per cent liable, and they paid 50 per cent of the claim, less the policy excess (net amount $10,774.64) to the liquidators. In a letter to Broadspectrum dated 15 September 2016, the liquidators said that they had received the $10,774.64, and that "the Liquidators offer this as settlement for [Broadspectrum's $36,549.27 claim]…".

[13] The third and last component of the Fund is a sum of $20,000 recovered by the liquidators from a shareholder of Stages, in settlement of the shareholder's overdrawn current account.

The financial position of Stages at and after the liquidation date

[14] By far the largest creditor of Stages was Heartland. Immediately after the liquidation, it served a demand on the liquidators for payment of the sum of $1,216,263.01. That amount was made up of $1,208,230.11 owing under a term loan agreement dated June 2014 (the TLA), and $8,032.90 owing under a commercial rental agreement.

[15] Following their appointment, the liquidators sold Stages' plant and equipment, and paid Heartland $895,665.39 on account of the amount owing to it. Heartland allowed the liquidators to act as its collection agents for that purpose, and it permitted the liquidators to deduct reasonable selvage costs. Heartland was happy with that process, and there is no issue between Heartland and the liquidators over the sale of the plant and equipment and the subsequent accounting to Heartland for the proceeds.

[16] As at the date of the liquidators' application for directions, the sum of $303,656.25 remained owing to Heartland under the TLA. The only remaining asset in the liquidation is the Fund.

[17] The preferential creditors are Stages' former employees, who have preferential wages or salary claims totalling $65,493.30, and the Inland Revenue Department,

which is owed a total of $380,301.89 for GST, PAYE, and employer contributions due by Stages in respect of child support payments.[1] As the Fund is the only remaining asset in the liquidation, there will be no money for the preferential creditors if Heartland's contention that its security interest (or its claim that the assets comprising the Fund are owned by it, not Stages) gives it priority is correct.

Heartland's securities

[18] Heartland has a security interest in Stages' accounts receivable, under an Invoice Financing Facility Agreement (the IFFA) and a Specific Security Deed (the SSD). The IFFA and the SSD were both dated 15 January 2007, and the named secured party was Marac Finance Ltd. Marac Finance Ltd amalgamated with Heartland on 1 December 2013 to form Heartland.

[19] It is common ground that Heartland's security interest under the IFFA and the SSD was perfected under the Personal Property Securities Act 1993 (the PPSA) prior to the liquidation, and there is no dispute over the validity of Heartland's security interest.

Section 312 and cl 2 of Schedule 7 of the Act

[20] The dispute between the parties is over the effect of certain provisions in s 312 and in cl 2 of Schedule 7 to the Act, and in particular whether those provisions entitle the former employees and the Commissioner of Inland Revenue to priority over Heartland in the distribution of the Fund.

[21] Section 312 of the Act deals with preferential claims. It provides that the liquidator must pay out of the assets of the company the expenses, fees, and claims set out in Schedule 7 to the Act to the extent and in the order of priority specified in that Schedule.

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[1] Under cl 1(2) of Schedule 7 to the Act, unpaid employees of a company in liquidation are preferential creditors in respect of wages or salaries for the four month period before the commencement of the liquidation. Under the same clause of Schedule 7, the Commissioner of Inland Revenue is entitled to preference in respect of certain unpaid taxes, including GST, PAYE, and unpaid amounts under the Child Support Act 1991.

[22] Section 312 goes on to provide that, without limiting cl 2(1)(b) of Schedule 7 to the Act, the term "assets" in s 312(1) does not include assets subject to a charge unless the charge is surrendered or taken to be surrendered or redeemed under s 305 of the Act.

[23] Clause 2 of Schedule 7 provides that preferential claims such as those of the former employees and the Commissioner in this case must be paid in full, unless the assets of the company are insufficient to meet them, in which case they abate in equal proportions.

[24] Clause 2 then goes on to provide:

> **2 Conditions to priority of payments to preferential creditors**
>
> (1) The claims listed in each of subclauses (2), (3), (4), and (5) of clause 1 [which include claims of the kind made by the former employees and the Commissioner in this case]—
>
> (a) rank equally among themselves … and
>
> (b) in so far as the assets of the company available for payment of those claims are insufficient to meet them,—
>
> (i) have priority over the claims of any person under a security interest to the extent that the security interest—
>
> (A) is over all or any part of the company's accounts receivable and inventory or all or any part of either of them; and
>
> (B) is not a purchase money security interest that has been perfected at the time specified in section 74 of the Personal Property Securities Act 1999; and
>
> (C) is not a security interest that has been perfected under the Personal Property Securities Act 1999 at the commencement of the liquidation and that arises from the transfer of an account receivable for which new value is provided by the transferee for the acquisition of that account receivable (whether or not the transfer of the account receivable secures payment or performance of an obligation); and

(ii) must be paid accordingly out of any accounts receivable or inventory subject to that security interest (or their proceeds).

(2) For the purposes of subclause (1)(b), the terms account receivable, inventory, new value, proceeds, purchase money security interest, and security interest have the same meanings as in the Personal Property Securities Act 1999.

(3) To the extent that the claims to which subclause (1) applies are paid out of assets referred to in paragraph (b) of that subclause, the amount so paid is an unsecured debt due by the company to the secured party.

…

The application for directions

[25] The liquidators apply for directions under s 284 of the Act. That section materially provides:

284 Court supervision of liquidation

(1) On the application of the liquidator, … the court may—

(a) give directions in relation to any matter arising in connection with the liquidation:

…

[26] In their application, the liquidators ask for the following directions:

1.1 That the sum of $89,712.14 ("Fund"), being the amount net of GST recovered by them as liquidators of [Stages] from accounts receivable of [Stages] is, after deduction of the liquidators' costs, to be applied to meet preferential creditor claims by employees of [Stages] and by Inland Revenue ("the Preferential Creditors") pursuant to cl 1(2) to 1(5) of Schedule 7 of [the Act];

1.2 In the alternative to 1.1 above, that the Preferential Creditors have priority over [Heartland's] security interest over [Stages'] accounts receivable;

1.3 That [Heartland] pays [the liquidators'] costs on a 2B basis, together with their reasonable disbursements.

Heartland's notice of opposition

[27] Heartland opposes all of the orders sought by the liquidators. I will address the various issues raised by Heartland in its notice of opposition later in this judgment.

Heartland's facilities

[28] Heartland's facilities were described by Mr Sean McMillan, its business asset manager.

[29] Mr McMillan said that, when Heartland enters into a factoring arrangement, two documents are generally executed. The first is an invoice finance facility agreement (an "iffa"). An iffa has three essential components, being a credit facility, an assignment of accounts receivable, and a security interest over accounts receivable. The second document is a specific security deed (an "ssd") over accounts receivable. As with an iffa, an ssd incorporates an assignment of accounts receivable and a security interest over accounts receivable.

[30] Both an iffa and an ssd secure all obligations owed by the client to Heartland. In this case, that included Stages' obligations under the TLA.

[31] The moment a debt comes into existence, the borrower grants a security interest in the debt to Heartland. Simultaneously, it transfers title in the debt itself by assigning all its right, title and interest in all debts to Heartland.

[32] Clause 5.1 of the IFFA in this case provided:

> **5 Security and Transfer**
>
> 5.1 **Security and transfer:** To secure due payment of the Outstanding Moneys and the observance and performance of the respective Obligations of [Stages] under the Relevant Documents, [Stages] grants to [Heartland] a security interest in all the Debts and transfers to [Heartland] all its right, title and interest (present and future, legal and equitable) in and to all Debts which are in existence at the date of [the IFFA] or which come into existence at any time thereafter.

[33] Mr McMillan explained how Heartland's factoring arrangements work in practice, as follows.

[34] Heartland uses a software solution known has "Hermes", which is installed on the borrower's (in this case Stages') database and connected to its accounting package. Under an iffa, the borrower assigns all its right, title and interests in all debts to Heartland. The borrower is appointed Heartland's collection agent in respect of the

debts, and it accepts that the security interest in the debts (created by the iffa and the ssd) secures all obligations of the borrower to Heartland.

[35] Relevant to the application of cl 2(1)(b)(i)(C) of the Act in this case, the borrower in an iffa accepts that "new value" is provided by Heartland in respect of each debt that is created when the borrower issues an invoice to a customer. Such a provision was included in the IFFA in this case at cl 5.5.

[36] A similar provision appeared at cl 3.2 of the SSD.

[37] The borrower under an iffa confirms that an account debtor does not have a right of set-off, and that the borrower will not negotiate any variation or release of the debt without obtaining Heartland's consent. The representations and warranties given by the borrower are continuous, and are given in respect of each debt which comes into existence. The borrower accepts that it will use the Hermes software, and that all payments in relation to each debt are redirected to Heartland's account.

[38] Mr McMillan explained that Hermes extracts all invoices/credit notes/cash receipts/journal entries processed in the borrower's accounting system, and that financial data is fed through and posted to the borrower's facility in Heartland's IFACTOR software. IFACTOR analyses the data, enabling both the borrower and Heartland to have an instant, real time, snapshot of the borrower's facility. The borrower is obliged to keep the information up to date, and that enables the IFACTOR software to undertake an automatic analysis of the financial data at least daily. Through the use of Hermes, Heartland holds all ledger transactions in IFACTOR, effectively holding a mirror version of the borrower's aged receivables ledger.

[39] Heartland has the ability to manually interrupt transactions from feeding through and updating the facility, instantly. For example, where a borrower has received a cheque which has been deposited to the borrower's account but has not yet cleared, Heartland can suspend IFACTOR until IFACTOR actually confirms that the amount deposited can be treated as cleared funds. Also, Heartland can disapprove specific debtors or invoices, in accordance with its own risk controls. Any invoice picked up in IFACTOR in this category is posted to the "non-approved ledger

balance". The risk controls entered into Heartland's IFACTOR system then apply automatically to reflect the non-approved item in the borrower's ledger balances.

[40] Heartland has a formula (based on a certain percentage of the current total approved aged receivables ledger) that it uses to calculate the funding available to the borrower from time to time, and the borrower is able to draw funds in accordance with that formula, up to the facility limit.

[41] Account debtors make payment of invoices issued by the borrower into Heartland's bank account for the borrower, and certain credit balances in that account are "swept" over to Heartland on a daily basis.

[42] Referring to the IFFA specifically, statements produced by Mr McMillan show that, as at 31 August 2015, Stages' debtors had paid a total of $349,340.64 into the Heartland account since 6 August 2015. A further $47,600 was paid by Heartland to Stages on 31 August 2015, and, with additional charges, the balance owing by Stages to Heartland at 31 August was $31,265.93.

[43] While Heartland made some further payments to Stages under the IFFA in early September 2015, the statements produced by Mr McMillan show that the small balance owing under the IFFA was cleared at or about the liquidation date.

[44] In a supplementary affidavit which was produced without objection at the hearing, Mr McMillan provided copies of printouts for the IFFA transactions between June and July 2015. The statements show cash received into Heartland's account during those months, and payments made by Heartland to Stages. The June 2015 statement shows that Heartland made numerous payments to Stages under the IFFA, including a payment of $50,000 on 30 June 2015. Similarly, the July statement records that Heartland made multiple payments to Stages under the IFFA during that month.

Factoring facilities generally

[45] In her submissions for Heartland, Ms Wakelin distinguished between the two common types of factoring arrangement, namely a "whole turnover factoring arrangement" and a "facultative factoring arrangement". In a facultative factoring

arrangement, debts are offered, accepted or declined by the financier on an individualised basis. The client's obligation is to offer each of its debts to the factor, which may accept or decline the particular debt. In a whole turnover factoring arrangement, every trade debt in existence at the start date and every trade debt that comes into existence during the currency of the agreement, is instantly vested in the factor (in this case Heartland) as soon as it comes into existence, without any further formality or other document evidencing the assignment of the debt to the factor.

[46] The two common types of factoring arrangements were described by Hammond J in *Commercial Factors v Maxwell Printing*, in the following terms:[2]

> … Essentially there are two types of factoring agreements. Facultative agreements have been the most common type. The term is used because, although the client is bound to offer every debt arising from sales in the ordinary course of its business, the factor may accept or decline to accept any debt. The arrangement is thus an optional one, and the factoring agreement operates as an umbrella. The absolute right to decline a debt has historically been thought to give a factor improved security.
>
> The second kind of commonly used agreement is a whole turnover agreement. The reluctance of the common law to recognise a present assignment of future property is well known. But equity has adopted a more sensible stance through its long recognition of that as being done which ought to be done. It is possible to construct (although real care is required in this respect) an agreement to assign debts as they come into existence without further formalities. Thus it is possible to have a whole turnover agreement catching payments as they fall in. But since those debts are turned over under a present assignment of future debts, the rights of the factor to the debt take effect as from the date of the agreement. This can produce an acceptable position for the factor in relation to set-offs … [citations omitted].

[47] Ms Wakelin submitted that we are here concerned with a whole turnover factoring arrangement, under which consideration was provided by Heartland as soon as the initial advance under the IFFA was made. The consideration was then "recycled" every day that the IFFA was not withdrawn.

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2 *Commercial Factors v Maxwell Printing* [1994] 1 NZLR 724 at 727.

The issues to be decided

[48] The following issues arise:

(1) Were all the components of the Fund assigned by Stages to Heartland absolutely, with the effect that they are assets of Heartland (and not Stages) to which s 312 and Schedule 7 of the Act cannot apply?

(2) If the answer to Issue (1) is "no", do the items comprising the Fund all constitute the realisation of "accounts receivable", or "inventory"?

(3) If and to the extent the components of the Fund represent the realisation of Stages' accounts receivable:

(i) did Heartland have a perfected security interest over the accounts receivable at the commencement of the liquidation?

(ii) if so, did Heartland's security interest over each account receivable arise from the transfer of that account receivable to Heartland?

(iii) if it did, are the liquidators constrained by the acknowledgments given by Stages at cls 5.5 of the IFFA and 3.2 of the SSD from contending that new value was not provided by Heartland for the acquisition of each account receivable?

(iv) if the Liquidators are not so constrained, did Heartland provide "new value" for the acquisition of each account receivable? What was the nature of any new value provided?

(v) if Heartland does hold a security interest in the accounts receivable of the kind described at cl 2(1)(b)(i)(C) of Schedule 7 of the Act, so that it was entitled to the accounts receivable in priority to the preferential creditors:

(a) does Heartland's security interest secure the balance owing on the TLA (when the amount owing under the IFFA was repaid in full by the liquidation date)?

(b) is Heartland's priority limited to the amount of the "new value" it provided to acquire the accounts receivable?

(4) In what capacity have the liquidators dealt with the assigned invoices, and at what point did their authority to do so cease?

(5) Can the liquidators deduct their fees (other than reasonable salvage costs incurred in recovering the accounts receivable) from the Fund?

[49] I will address each of those issues in turn.

Issue (1) — Were all the components of the Fund assigned by Stages to Heartland absolutely, with the effect that they are assets of Heartland (and not Stages) to which s 312 and Schedule 7 of the Act cannot apply?

Submissions for Heartland

[50] Ms Wakelin submitted that Schedule 7 of the Act only applies to assets of the company in liquidation. The debts owed by Broadspectrum and the shareholder immediately became assets of Heartland, and as such they cannot be available for the preferential creditors or for the liquidators' costs (subject to reasonable "salvage costs" of recovering the funds from Broadspectrum and the shareholder).

[51] Section 50 of the Property Law Act 2007 (the PLA) recognises the absolute nature of an assignment of the kind made by Stages in this case. It provides that, following the assignment, all rights "in relation to the thing" pass to the assignee (in this case, Heartland). It would be a perverse result if assets, which at law belonged to Heartland, were nevertheless available to the liquidators to distribute amongst the preferential creditors. If that were the case, the liquidators' interpretation of the PPSA would be directly in conflict with both the Act (s 312 and Schedule 7) and s 50 of the PLA. If Parliament had intended the PPSA to prevail over both the Act and the PLA, clear and unambiguous language would have been used, but it was not.

[52] Ms Wakelin submitted that, while ownership may not be determinative for the purpose of determining competing priorities between the holders of security interests, that is as far as the limitation on the primacy of legal title goes. It was not intended to be applied to determine a contest between the owner of accounts receivable under an absolute assignment from the company in liquidation and preferential creditors in the liquidation. She referred in support to the following passage in *New Zealand Bloodstock Ltd v Waller*, where the majority of the Court of Appeal said:[3]

> (a) The lease to purchase being for more than one year, *for the limited purpose of fixing priorities of competing proprietary interests,* New Zealand Bloodstock's title became a "security interest" (s 17(1)(b)). [Emphasis added.]

[53] That qualification was said to have been repeated later in the same judgment, in these terms:[4]

> Such conclusion means that with respect to priority of competing security interests under the PPSA the *nemo dat* principle is ousted. The consequence is to empower Glenmorgan to add to the security passing to Lock under Lock's debenture a proprietary interest in the stallion, even though the agreement between New Zealand Bloodstock and Glenmorgan had provided to the contrary. We therefore reach the same conclusion on the appeal as Allan J for like reasons.

Submissions for the liquidators

[54] Mr Crombie acknowledged that the four Broadspectrum invoices were assigned automatically and absolutely to Heartland under cl 5.1 of the IFFA. But notwithstanding the absolute nature of the assignment, the transfer of the accounts receivable is still deemed to be a security interest under s 17(1)(b) of the PPSA. That section materially provides:

> **17 Meaning of security interest**
>
> (1) In this Act, unless the context otherwise requires, the term **security interest**—
>
> …
>
> (b) includes an interest created or provided for by a transfer of an account receivable or chattel paper, a lease for a term of more

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3 *Waller v New Zealand Bloodstock Ltd* [2006] 3 NZLR 629; (2005) 9 NZCLC 263,944; (2005) 11 TCLR 497; (2005) 2 NZCCLR 985, at [51(a)].

4 At [74].

> than 1 year, and a commercial consignment (whether or not the transfer, lease, or consignment secures payment or performance of an obligation).

…

[55] Even though Stages' interest in the invoices passed to Heartland, the PPSA priority regime still applies.

[56] That is also the position under Schedule 7 to the Act, which imports into the Schedule the meanings of certain terms as used in the PPSA. The expressions "account receivable", "new value", and "purchase money security interest", are all defined in s 16 of the PPSA, and the definition of "security interest" in s 17 of the PPSA catches an outright sale of accounts receivable, such as the assignment of future debts which the IFFA effected or provided for in this case.[5]

Discussion and conclusions on Issue (1)

[57] I accept Mr Crombie's submissions on this issue.

[58] Under s 17(1)(b) of the PPSA, the term "security interest" includes an interest created or provided for by a transfer of an account receivable, [6] and I think in this case it is clear that the SSD created an interest in Stages' accounts receivable. That interest was provided for by the requirements of the IFFA for transfer of the accounts receivable to Heartland. Section 17 of the PPSA does not distinguish between an absolute assignment of an account receivable (the situation here) and a charge or security over the account receivable that provides for such an assignment; the effect of the section is that even an absolute transfer or assignment of an account receivable is deemed to be a security interest for the purposes of the PPSA.

[59] The learned authors of *The Personal Property Securities Act 1999: Act & Analysis* put the matter this way:[7]

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5 Blanchard and Gedye, *Private Receivers of Companies in New Zealand* (Lexis Nexis) at 5.09, and Barry Allan, *The Law of Secured Credit* (Thomson Reuters, Wellington, 2016) at 12.4.02.

6 The expression "account receivable" is defined in s 16 of the PPSA as meaning "a monetary obligation that is not evidenced by chattel paper, an investment security, or by a negotiable instrument, whether or not that obligation has been earned by performance".

7 Barry Allan *The Personal Property Securities Act 1999: Act & Analysis* (Thomson Reuters, Wellington 2010) at 132 to 133.

> Accounts receivable are a very significant asset … Debtors want to expedite the payment each represents, and so they will either sell them outright or use them as collateral for borrowing. Both situations are rendered into deemed security interests by s 17(1)(b), meaning that even a buyer of accounts receivable (outside those excluded by s 23) is dependent for its priority upon the PPSA. While it is recognised that a factor is someone who takes an absolute assignment of account, ie a sale, rather than one which is an assignment pursuant to a security arrangement, the discussion in this context will use factor and assignee interchangeably, given that [the PPSA] makes no distinction.
>
> …
>
> Any transfer of an account receivable is a deemed security interest (unless excepted by s 23).

[60] The learned authors of *Private Receivers of Companies in New Zealand* take the same view: s 17 brings factoring agreements and assignments of accounts receivable in outright form within the PPSA regime.[8]

[61] Section 23 of the PPSA does not apply on the facts of this case, and accordingly I do not consider that Heartland's legal ownership of the accounts receivable comprised in the invoices Stages sent to Broadspectrum assists Heartland. Heartland's ownership interest in those accounts receivable is deemed to be subject to the specific requirements of s 17(1)(b) of the PPSA and cl 2(1)(b)(i) of Schedule 7 of the Act.

[62] I do not think that either of the passages from *Waller* referred to by Ms Wakelin assists Heartland. In respect of the passage quoted at [52] of this judgment , it is by no means clear that the majority intended that the "limited purpose" referred to excluded the situation where the competing parties were the holder of a security interest under the PPSA and preferential creditors with statutory entitlements under cl 2(1)(b) of Schedule 7 of the Act. The majority was concerned with fixing priorities between competing parties, one of whom had an ownership interest in the asset in question while the other held a security interest (a debenture) in it, registered under the PPSA. For the limited purpose of priority of securities, the contractual language under which the respondent held title to the asset was overridden by the wording of s 17 of the PPSA. In my view the legislature's decision to import the various PPSA definitions into cl 2 of Schedule 7 makes it clear that the same legislative policy choice

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8 Blanchard and Gedye, *Private Receivers of Companies in New Zealand*, above n 5, at 5.09.

was intended where the "limited purpose" was to determine priorities as between the holder of a security interest (who happens to have title to the asset in question) and the preferential creditors with statutory rights under cl 2(1)(b). Whether the holder of the security interest in the accounts receivable had legal title to them, would not be relevant. The second passage from *Waller* to which Ms Wakelin referred (quoted at [53] above) does not detract from that view. It does no more than establish that, with respect to priority of competing security interests under the PPSA, the *nemo dat quod non habet* principle[9] is ousted. That it is no more than a qualification on the primacy of title that is accepted by Mr Crombie. The issue here is whether that qualification was intended to apply in the context of cl 2(1)(b) of Schedule 7 of the Act, and I am satisfied that it was.

[63] Further, in *Strategic Finance Ltd (In Liquidation) v Bridgman*, the Court of Appeal said:[10]

> … The current wording was enacted to ensure that the availability of "accounts receivable" for preferential creditors would not be dependent on the wording of the particular instrument which creates the security interest.

[64] While that passage was concerned with the effect of the PPSA's abolition of the earlier distinction between fixed and floating charges and not (directly) with the distinction between a factor who has taken an absolute assignment of accounts receivable and one who merely holds a charge over the receivables, I think it tends to support Mr Crombie's submission that the position of preferential creditors in respect of accounts receivable does not depend on the particular form of security interest over the accounts receivable that a factor might hold (whether chargeholder or assignee under a sale or outright assignment).

[65] Turning to Ms Wakelin's argument based on conflict with s 50 of the PLA, I acknowledge the apparent conflict. It is referred to in *The Law of Secured Credit* in the following terms:[11]

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9 Where property in goods has not passed to the buyer, subject to certain exceptions, he or she cannot confer a good title on a sub-buyer … no one can give a better title than he or she possesses. (*Waller v New Zealand Bloodstock Ltd*, above n 8 at [52].)

10 *Strategic Finance Ltd (In Liquidation) v Bridgman* [2013] NZCA 357, at [73].

11 Barry Allan, *The Law of Secured Credit* (Thomson Reuters, Wellington, 2016) at 12.4.02.

> A possible conflict arises between s 50 of the Property Law Act 2007 and the PPSA, as s 50(1) states than an "absolute assignment" of accounts receivable, so long as the [writing] requirements are satisfied, passes all of the assignor's rights to the assignee. This suggests that the assignee need not be concerned with perfection to protect its position. The Ontario Court of Appeal in *Fairbanx Corp v Royal Bank* noted a similar conflict between Ontario's PPS legislation and the equivalent to s 50, which was resolved by a provision in the PPS legislation giving precedence to the other Act. The Australian PPSA has a similar rule in s 254, but New Zealand lacks an equivalent provision: s 78 of the Property Law Act 2007 allows a conflicting PPSA provision to prevail, but only in relation to pt 3 of the 2007 Act, which does not include s 50. The intent of the PPSA that an absolute transfer of accounts receivable is governed by the PPSA is so clear that the conflict is necessarily resolved in favour of the PPSA prevailing.
>
> (Citations omitted.)

[66] I agree with the view of Mr Allan that the intent of the PPSA that an absolute transfer of accounts receivable is governed by the PPSA is so clear that the conflict is necessarily resolved in favour of the PPSA prevailing. In my view the broad general provisions of s 50 of the PLA, which apply generally to assignments, do not derogate from the very specific provisions of the PPSA and cl 2(1)(b)(i) of Schedule 7 to the Act relating to the priority of claims in a liquidation as between preferential creditors and those holding security interests over accounts receivable. Once Stages went into liquidation, and the question arose as to who had priority over the accounts receivable, the specific provisions of the PPSA and cl 2(1)(b)(i) of Schedule 7 were intended to apply. Title is not determinative under the PPSA, and the meaning of "security interest" as that expression is used in the PPSA is expressly imported into cl 2(1)(b)(i) of Schedule 7 of the Act.[12] Heartland could be in no better position than (a non-owning) holder of a security interest in the relevant accounts receivable.

[67] Turning to Ms Wakelin's argument based on s 312 of the Act, which provides that the liquidator must pay out of the assets of the company the expenses, fees, and claims set out in Schedule 7 of the Act, the section also provides that the Schedule applies to the payment of those expenses, fees, and claims "according to its tenor". The primary purpose of s 312 is to impose obligations on the liquidator as to the payment of certain expenses fees and claims in priority to other claims in the liquidation, and Schedule 7 is to be applied towards that purpose. The starting point

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[12] *Strategic Finance Ltd (in receivership and in liquidation) v Bridgman* [2013] NZCA 357; [2013] 3 NZLR 650, at [48]-[50].

under s 312(1) will be that the preferential expenses fees and claims are to be paid out of assets owned by the company, but if there are no such assets or they are insufficient to meet those expenses fees and claims, the Schedule is to be applied "according to its tenor".

[68] The opening words of cl 2(1)(b) of Schedule 7 expressly address the position where the assets of the company available for payment of the preferential expenses fees and claims are insufficient to meet them, and cl 2(1)(b) goes on to provide that the expenses fees and claims may be paid from the company's accounts receivable (in priority to the holder of a security interest in the accounts receivable) if the circumstances set out at subparagraphs (A), (B) and (C) of cl 2(1)(b)(ii) are all present. The effect of importing the PPSA definition of "security interest" into the cl 2(1)(b) regime is that the regime applies whether the company or the holder of the security interest is the legal owner of the accounts receivable. "Security interest" in the PPSA is defined to include the situation where there has been an outright sale or assignment of the accounts receivable, and the words in cl 2(1)(b)(i): "have priority over the claims of any person *under a security interest* to the extent that *the security interest* …" (emphasis added) must therefore be equally applicable where the security interest has been created or provides for the holder to take an outright assignment or transfer of the accounts receivable.

[69] I do not consider that s 312(2) affects that view, as the subsection is clearly to be read subject to cl 2(1)(b) of Schedule 7.

[70] I conclude on Issue (1) that although the relevant invoices were assigned absolutely to Heartland pursuant to the IFFA and the SSD, they nevertheless remained "accounts receivable", and were available to meet preferential payment claims under the provisions of cl 2(1)(b) of Schedule 7, if the requirements of cl 2(1)(b)(i)(A), (B) and (C) were all met.

Issue (2) — If the answer to Issue (1) is "no", do the items comprising the Fund all constitute the realisation of "accounts receivable", or "inventory"?

[71] As far as the evidence shows, I am not here concerned with "inventory". Under cl 2(2) of Schedule 7 of the Act and s 16 of the PPSA, "inventory" means "goods" (that

meet the requirements of the s 16 definition), and I am concerned here with debts owed to Stages for services provided (the subject of the four invoices) or on a current account (the $20,000 owing on the shareholder's current account with Stages). The amount received on the insurance claim was not "goods".

[72] There is no dispute that the three invoices raised by Stages before the liquidation created "accounts receivable". To the extent they are now represented in the Fund, the Fund consists of the proceeds of these invoices. Any security interest held by Heartland will extend to those proceeds.[13]

[73] The position is not so clear with the other assets that make up the Fund. I consider first the fourth invoice for $105,372.20, issued by the liquidators over a year after the liquidation.

[74] "Accounts receivable" is defined in the PPSA as:

> … a monetary obligation that is not evidenced by a chattel paper, an investment security, or by negotiable instrument, whether or not that obligation has been earned by performance.

[75] That definition is imported into cl 2 of Schedule 7 by cl 2(2) of the Schedule.

[76] There is no question here of any "chattel paper", "investment security" or "negotiable instrument".

[77] In *Strategic Finance*, the Court of Appeal confirmed that "accounts receivable" as defined in s 16 of the PPSA and cl 2(2) of Schedule 7 of the Act is not limited to a company's book debts.[14] The Court went on to say:[15]

> "Monetary obligation" in the context of the PPSA means an existing obligation imposed upon, or assumed by, one party to pay a certain sum of money to the other party on a specific or ascertainable future date. An obligation of this nature will involve an existing liability enforceable by the second party …
>
> … For an amount to be "receivable", it must be currently owed to a party who is entitled to expect its payment without undertaking further performance.

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13 Section 45(1)(b) of the PPSA.
14 *Strategic Finance Ltd (in receivership and in liquidation) v Bridgman*, above n 10, at [52].
15 At [54] and [60].

[78] Priorities between competing claims are to be determined as at the date of liquidation,[16] and I think that means the account receivable must be in existence at the date of the liquidation. That is not the case in respect of the fourth invoice — it appears that all there would have been at the liquidation date was unbilled work in progress, which could not have created any existing obligation on Broadspectrum to pay. I accordingly find that the amount recovered on the fourth invoice, to the extent it is represented in the Fund, does not represent the realisation of an "account receivable" for the purpose of cl 2(1)(b)(i)(A) of Schedule 7. There was no relevant "account receivable" in existence at the liquidation date from which the claims of the preferential creditors could be paid under cl 2(1)(b)(ii).

[79] I see no reason why the $20,000 owing on the shareholder's current account does not qualify as an "account receivable". It was clearly a monetary obligation on the shareholder to pay a certain sum of money to Stages, and it appears to have been payable upon demand. The Court held in *Strategic Finance* that money held in a bank account, or in a solicitor's trust account, is payable on a sufficiently specific or ascertainable future date (when the account-holder or client asks for the money), and it seems to me that the position should be no different for a current account debt owed by a shareholder to his or her company which is payable upon demand. I find that the $20,000 debt owed by the shareholder was an "account receivable" for the purpose of cl 2 of Schedule 7 of the Act.

[80] Turning to the insurance claim ($10,774), I am prepared to infer from the liquidator's letter of 15 September 2016 and the apparent absence of any response from Broadspectrum that Broadspectrum agreed that these funds should be treated as a payment on account of its agreed (net) obligations on the four invoices issued by Stages and the liquidators. To the extent the payment was made on the three invoices issued by Stages before the liquidation, the payment involved the realisation of the three corresponding accounts receivable. If and to the extent it was a payment in reduction of the fourth invoice, it did not represent the realisation of any relevant account receivable.

16 At 86, referring to cl 6 of Schedule 7 of the Act.

Issue (3) — If and to the extent the components of the Fund represent the realisation of Stages' accounts receivable:

(i) did Heartland have a perfected security interest over the accounts receivable at the commencement of the liquidation?

[81] It is not in dispute that it did — the answer is "yes".

(ii) if so, did Heartland's security interest over each account receivable arise from the transfer of that account receivable to Heartland?

[82] Again, I do not understand there to be any dispute over this issue. As each account receivable was created it was automatically transferred to Heartland under cl 5.1 of the IFFA, and the purpose of the transfer was to secure the due payment of the "Outstanding Moneys" as defined in the IFFA. Heartland's interest was accordingly created or provided for by the transfer, in accordance with the definition of "security interest" in s 17(1)(b) of the PPSA. The answer to this Issue is "yes".

(iii) if it did, are the liquidators constrained by the acknowledgments given by Stages at cls 5.5 of the IFFA and 3.2 of the SSD from contending that new value was not provided by Heartland for the acquisition of each account receivable?

[83] Clause 5.5 of the IFFA and cl 3.2 of the SSD respectively provided:

> 5.5 **Value**: The Borrower agrees and acknowledges that new value for the purposes of clause 9(b)(i)(C) of the Seventh Schedule to the Companies Act 1993 is given by the Lender to the Borrower in respect of the Debt transferred to the Lender and/or over which the Lender holds a security interest pursuant to this Agreement, notwithstanding the amount of value given, date of Advance or date of Invoice.
>
> **3.2 Value:** The Debtor agrees and acknowledges that new value for the purposes of clause 9(b)(i)(C) of the Seventh Schedule to the Companies Act 1993 is given by the Secured Party to the Debtor in respect of each Contract transferred to the Lender and/or over which the Lender holds a security interest pursuant to the Invoice Finance Facility Agreement and this Deed, notwithstanding the amount of value given or the date of advance under the Invoice Finance Facility Agreement or the date of the Contract.

[84] Ms Wakelin submitted that these clauses give effect to the principle in s 50(4) of the PLA that where there has been an absolute assignment (as here), valuable consideration is deemed to have been provided. The "Value" clauses in the IFFA and

the SSD reflected the parties understanding and agreement that fresh new advances by Heartland would not necessarily be made against each invoice. The parties were recognising that this was a whole turnover factoring arrangement, and the "Value" clauses sought to avoid the very argument the liquidators now make on the "new value" issue. She submitted that the liquidators are bound by cl 5.5 of the IFFA and cl 3.2 of the SSD.

[85] Mr Crombie submitted that parties cannot contract out of the PPSA and Schedule 7 of the Act, and the "Value" acknowledgments are not binding unless the Court finds that "new value" has a meaning consistent with the acknowledgments.

[86] Mr Crombie also referred to *Strategic Finance*, where the Court of Appeal said:[17]

> … The current wording [of cl 7] was enacted to ensure that the availability of "accounts receivable" for preferential creditors would not be dependent on the wording of the particular instrument which creates the security interest. …

[87] I accept Mr Crombie's submission that the "Value" clauses do not preclude the liquidators from taking the position that no "new value" (as defined in the PPSA) was provided by Heartland.

[88] The parties to an agreement which creates or provides a security interest under the PPSA cannot provide their own definition of "new value" for the purposes of cl 2(1)(b)(i)(C) of Schedule 7 of the Act, if that definition is inconsistent with the definition of "new value" provided in s 16 of the PPSA. That is because s 312 of the Act and Schedule 7 create a set of rules for the payment of preferential expenses and claims in a liquidation, which a liquidator is bound to follow. Section 312 and Schedule 7 also create statutory rights for preferential creditors, and the parties to an agreement that creates or provides for a security interest cannot unilaterally remove or abrogate those rights. Therefore the question under cl 2(1)(b)(i)(C) will always be whether "new value" has been provided within the meaning of that expression as defined in s 16 of the PPSA, not as the parties may have chosen to define it.

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17 *Strategic Finance Ltd (In Liquidation) v Bridgman*, above n 9, at [73].

[89] That is consistent with the Court of Appeal's view in *Strategic Finance* that "the availability of "accounts receivable" for preferential creditors [is not to be] dependent on the wording of the particular instrument which creates the security interest".

[90] For those reasons, my answer to Issue (3)(iii) is "no".

(iv) if the Liquidators are not so constrained, did Heartland provide "new value" for the acquisition of each account receivable? What was the nature of any new value provided?

Submissions for Heartland

[91] The expression "new value" in the PPSA is defined to mean "value other than antecedent debt or liability". "Value" means "consideration that is sufficient to support a simple contract".

[92] Having regard to that definition of new value, Ms Wakelin submitted that there is no need for the Court to conduct any enquiry into the adequacy of the consideration provided by Heartland for the accounts receivable. She also referred to s 50(4) of the PLA, which provides:

> The priority of an assignment to which subsection (1) applies and which is not given for valuable consideration is to be determined as if the assignment had been given for valuable consideration.

[93] Ms Wakelin submitted that, in the present context, value becomes "new" when there is some degree of contemporaneity between Heartland continuing to make the IFFA available (and continuing to make advances under the IFFA), and/or Stages receiving the benefit of a better risk profile than it otherwise would have, at the point in time that the debts became Heartland's property. She submitted that Heartland gave "new value" in three separate respects. First, it provided daily consideration, in that the mechanics of the IFFA provided for daily recycling of the facility — each new day Heartland decided whether to leave the facility in place or to demand repayment. Secondly, Heartland provided new contractual consideration. It expressly agreed in the IFFA and the SSD that new value was given by Heartland to Stages in respect of the relevant debts. Thirdly, if new "cash" was required to be given, new value in that

form was provided. Ms Wakelin referred to the further payments made by Heartland to Stages between June and September 2015, as referred to at paragraphs [42] – [44] of this judgment.

Submissions for the liquidators

[94] Mr Crombie noted that the meaning of "new value" does not appear to have been considered by a senior court in this country. However, the meaning of "new value" has been considered by academic commentators in the context of its use in other sections of the PPSA, most notably s 75A (which is broadly concerned with priorities as between the holder of a security interest in accounts receivable, and the holder of a purchase money security interest (PPSI) over the company's inventory and any proceeds of sale thereof).

[95] Mr Crombie referred to the *Gault on Commercial Law*, where the learned author said the following of s 75A:[18]

> The reason for limiting this priority to those who provide new value is obvious: there is an expectation that the debtor's asset position will not deteriorate as a result of the factoring arrangements and it will have improved cashflow. A creditor which has already made advances cannot then take the accounts receivable (or security for them) to satisfy its advance and rely upon s 75A to give it priority.

[96] Mr Crombie also referred to *Heath & Whale on Insolvency*, where the learned authors express the view that, to achieve the result intended by s 75, the meaning of "new value" should be restricted to value given at the time the security interest in the account receivable attached and expressly for the specific purpose of acquiring the security interest in the account receivable.[19]

[97] The last of the text book references made by Mr Crombie on this issue was to *Private Receivers of Companies in New Zealand*, where the learned authors express the view that a receiver is unlikely to be able to rely on s 75A to defeat an inventory supplier's proceeds claim to accounts receivable. Although the holder of a general security interest of the type under which a receiver would likely have been appointed

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[18] *Gault on Commercial Law* (Thomson Reuters New Zealand) at 8A.4.04.

[19] *Heath & Whale on Insolvency* (online looseleaf ed Lexis Nexis, Wellington 2019) at 25.21(b).

would have a non-proceeds security interest in accounts receivable, it was considered unlikely that the secured party would have given "new value" as required by s 75A for the acquisition of the interest in the accounts receivable.[20] The authors of went on to note that:[21]

> … based on the statutory context and the Parliamentary history, … in s 75A "new value" means new value given specifically for the acquisition of an interest in the accounts receivable, such as when accounts receivable are purchased by factor. The alternative view is that "new value", as defined in s 16, simply means value given at the time or after a security agreement is entered into so that a general financier could also claim the benefit of s 75A.

[98] In summary, Mr Crombie submitted that new value must be given at the time the security interest in the accounts receivable attaches. That occurs at the time each invoice is issued by the company. Because new value does not include antecedent debt, the advances that Heartland made under the TLA in 2014 cannot be new value for the purposes of cl 2(1)(b)(i)(C) of Schedule 7.

Discussion and conclusions on Issue (3)(iv)

[99] First, I do not think any "new value" was provided by Heartland to acquire the $20,000 debt owed by the shareholder to Stages on his current account. I accept the view expressed by the learned authors of *Private Receivers of Companies in New Zealand* that "new value" under cl 2(1)(b)(i)(C) must be given specifically to acquire an interest in the particular account receivable, and I do not consider that was the case with the shareholder current account. There is no evidence that Stages invoiced the amount owed to the shareholder, and for that reason it would not have come within the definition of "Debt" in cl 1.1 of the IFFA. It therefore stood outside the IFFA, and effectively qualifies as an "account receivable" only in the same way a company's bank account, or money held for the company in its solicitor's trust account, so qualifies. I conclude that Heartland did not provide new value to acquire the shareholder's debt of $20,000, and that the preferential creditors have priority under cl 2(1)(b)(i) and (ii) as far as this account receivable is concerned.

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[20] Peter Blanchard and Michael Gedye *Private Receivers of Companies in New Zealand*, above n 5, at 5.10.

[21] At 5.10, footnote 8.

[100] Turning to the three invoices issued by Stages before the liquidation, I am satisfied that the amount advanced by Heartland under the TLA constituted "antecedent debt or liability", and so did not amount to the provision of "new value" for the purposes of cl 2(1)(b)(i)(C), and I have already rejected Ms Wakelin's submission based on "deemed new value" agreed under the IFFA. I doubt that simply refraining from making demand under the IFFA could have amounted to the provision of "new value" (particularly as the "refraining" would presumably not have been directed to the acquisition of any particular account receivable), and I also doubt that the fact that cash advances were in fact made by Heartland after the dates of the three invoices could have amounted to the provision of "new value". The provision of the new cash would seem to have not necessarily been referable to the acquisition of one or more of the three invoices. However, it seems to me that there might be another basis (to which neither counsel appears to have referred) on which Heartland could be said to have provided the necessary new value. Immediately the invoices were written and (automatically) assigned to Heartland, it might be that Stages did receive something of (new) value, namely an effective increase in the amount that would be available to it by way of advances from Heartland. Mr McMillan described the way the system operated as follows:

> 15. Funding is maintained for the borrower at a certain percentage of the current total approved aged receivables ledger. The figure is updated daily with information feeding in via Hermes at all times.
>
> 16. The calculation for funding available to the borrower [in this case Stages] at all times is …
>
> (current Approved Ledger x Advance percentage) – Current Facility Balance = Available Funds to Draw (up to the facility limit).

[101] It appears from that description that, each time an invoice was assigned by Stages, the "Current Approved Ledger" figure would probably have increased, thereby increasing (subject to the facility limit) the funds available for Stages to draw down under the facility. The IFFA does provide (at cl 2.1 – 2.2) that advancing funds under the IFFA was a matter for Heartland's discretion, but Heartland's overall responsibility under cl 2.1 was to "make available to [Stages] the Facility", and it was arguably not the intention of the parties that Heartland would take an outright assignment of all of the Debts and provide nothing in return.

[102] I would be grateful for further submissions from counsel on the question of whether Heartland provided "new value" to Stages to acquire each of the accounts receivable comprised in or arising from the three invoices issued by Stages to Broadspectrum before the liquidation, by effectively increasing the amount of credit available to Stages under the IFFA as and when each debt was assigned, by an amount referable to the amount of the assigned debt.

(v) if Heartland does hold a security interest in the accounts receivable of the kind described at cl 2(1)(b)(i)(C) of Schedule 7 of the Act, so that it was entitled to the accounts receivable in priority to the preferential creditors:

(a) does Heartland's security interest secure the balance owing on the TLA (when the amount owing under the IFFA was repaid in full by the liquidation date)?

(b) is Heartland's priority limited to the amount of the "new value" it provided to acquire the accounts receivable?

[103] I consider Issue (3)(v)(b) first.

Submissions for the liquidators

[104] Mr Crombie submitted that the key to answering Issue 3(v)(b) lies in the words "to the extent that" in the opening words of cl 2(1)(b)(i) of Schedule 7. He referred to the judgment of Fisher J in *Commissioner of Inland Revenue v Nicholls*, a case concerned with a taxpayer's right to deduct the full GST payable on an agreement to purchase land.[22] The relevant provision in the Goods and Services Tax Act provided that input tax could be deducted "to the extent that" the payment was made in respect of the supply. The Court held that the words "to the extent that" contemplated some form of apportionment.[23] Mr Crombie submitted that the words "to the extent" signal Parliament's intention that a security interest which arises from the transfer of an account receivable for which new value was given is to have priority over preferential creditor claims only to the extent of that new value.

[22] *Commissioner of Inland Revenue v Nicholls* (1997) 18 NZTC 13,265 (HC).
[23] At 6.

Submissions for Heartland

[105] Ms Wakelin focused on the wording of subclause 2(1)(b)(i)(C), submitting that the word "that" in the expression "provided by the transferee for the acquisition of *that* account receivable" (emphasis added) indicates connection or linkage between the specific "account receivable", and the new value provided as consideration. She then submitted that it is not possible to accurately quantify, in monetary terms, the value of the new consideration Heartland provided for the acquisition of each account receivable. For that reason, the Court should be slow to accept the submission that Heartland's priority ought to be limited to the amount of any "new value", or that "fractionalising" or some other method of apportionment should be adopted.

Discussion and conclusions on Issue 3(v)(b)

[106] First, the question raised by Issue (3)(v)(b) will only arise if, after considering counsel's further submissions on Issue 3(iv) referred to in [102] above, I conclude that Heartland did provide new value to acquire the accounts receivable created or arising from the three invoices issued by Stages before the liquidation. What follows is to be read subject to that proviso.

[107] I accept that the words "to the extent that" in the opening part of cl 2(1)(b)(i) qualify the words in subclause (i)(C) "… is not a security interest that … arises from the transfer of an account receivable for which new value is provided …". But in my view the words "to the extent that" in the introductory part of subclause 2(1)(b)(i) are concerned only with the *kind* of security interest over which preferential creditors are to have priority. "To the extent" in this context is directed to the question of whether the relevant security interest is of a kind which comes within all three of subclauses (A), (B) and (C) in cl 2(1)(b)(i), and the security interest will either come within subclause (C) or it will not. In my view treating the expression "new value" as it is used in subclause (C) as requiring or permitting the kind of "fractionalising" for which Mr Crombie contended would have required additional language in subclause (C) which is simply not there. The only relevant requirement in subclause (C) is that the perfected security interest in the account receivable must not have arisen from a particular kind of transfer (ie, one for which new value has been provided for the acquisition of the account receivable).

[108] I accept Ms Wakelin's submission, substantially based upon the definitions of "new value" and "value" in the PPSA, that it would often not be practical or possible to easily put a monetary figure on the "new value" provided by the transferee, and in the context of a statutory regime intended to be applied by busy liquidators it is unlikely that the regime was intended to require liquidators to embark on a potentially complex issue of assessing that figure.

[109] I accept that situations might arise on that interpretation where a creditor who is owed a substantial sum by a company might take a security interest in one or more of the company's accounts receivable on payment of a nominal amount of new consideration (eg $1.00). On the interpretation of cl 2(1)(b) to which I have come, that would be sufficient to secure priority over preferential creditors in a liquidation. But if such a transaction took place close enough to liquidation date the liquidator might have other remedies available to him or her under the Act (for example, remedies based on transfer of an asset of the company at an under value).

[110] For those reasons, I answer Issue 3(v)(b) by saying that, if and to the extent Heartland did provide new value to acquire the accounts receivable created by or arising from the three invoices issued by Stages before the liquidation, Heartland's priority over the preferential creditors under cl 2(1)(b)(i) is not limited to the amount of the "new value" it provided to acquire each of those three accounts receivable.

Discussion and conclusions on Issue (3)(v)(a)

[111] Turning to Issue 3(v)(a), the answer is that, if and to the extent Heartland did provide new value to acquire the accounts receivable created by or arising from the three invoices issued by Stages before the liquidation, Heartland's security interest in those three accounts receivable did and does secure the balance owing on the TLA, in priority to the preferential creditors' claims under cl 2(1)(b)(i) and (ii). The SSD over the accounts receivable secured due payment of the "Secured Indebtedness", and that expression was defined to mean all indebtedness of Stages to Heartland. Thus the amounts advanced under the TLA would be covered by the security interest if new value was sufficiently provided. The fact that some of the indebtedness secured by the security interest might have been repaid by the liquidation date (ie the amounts

advanced by Heartland under the IFFA) would not in my view affect any entitlement of Heartland to enforce its security interest over the three accounts receivable in respect of that part of the Secured Indebtedness that had not been repaid.

Issue (4) — In what capacity have the liquidators dealt with the assigned invoices, and at what point did their authority to do so cease?

Submissions for the liquidators

[112] Mr Crombie relied on s 102(1) of the PPSA. That section materially provides:

> **102 Priority of interests on assignment of account receivable or chattel paper**
>
> (1) The rights of an assignee of an account receivable or chattel paper are subject to—
>
> (a) the terms of the contract between the account debtor and the assignor and any defence or claim arising from the contract or a closely connected contract; and
>
> (b) any other defence or claim of the account debtor against the assignor (including a defence by way of a right of set-off) that accrues before the account debtor acquires knowledge of the assignment.
>
> (2) Subsection (1) does not apply if the account debtor on an account receivable or chattel paper has made an enforceable agreement not to assert defences to claims arising out of the contract.
>
> …

[113] Mr Crombie referred to *Gault on Commercial Law*, and the following commentary in relation to s 102 of the PPSA:[24]

> This does mean that in respect of a particular receivable, an account debtor is entitled to set-off claims that arise under a specific contract, but also those closely connected to it … These entitlements of the account debtor against the assignee continue despite knowledge of assignment by the account debtor, in the sense that even if they accrue after assignment and knowledge of it, the account debtor can still rely upon them as a set-off. The only way in which an assignee can avoid them is if the account debtor has made an enforceable agreement not to assert its rights, which is permissible under s 102(2). …

[114] In this case, Broadspectrum did not make any agreement not to assert any defences it might have to Stages' claims, so s 102(2) does not apply. The result is that

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[24] *Gault on Commercial Law* (Thomson Reuters New Zealand) at 8A.4.04(2).

the rights of Heartland as the assignee were subject to the terms of the contract between Broadspectrum (as account debtor) and Stages (as assignor of the Broadspectrum debts).

[115] Mr Crombie then referred to s 310 of the Act, which broadly provides that where there have been mutual credits, debits or dealings between the company and another party, an account must be taken of what is due from one party to the other and an amount due from one party must be set-off against an amount due from the other. Only the balance may be claimed in the liquidation.

[116] Mr Crombie submitted that, of the three invoices itemised at paragraph [6] of this judgment (totalling $188,183.03), all but $11,158.09 was set-off against Broadspectrum's cross-claims in the agreement reached between the liquidators and Broadspectrum. The liquidators were entitled to agree on the set-off under s 102(1) of the PPSA and s 310 of the Act, and the result is that even if Heartland did provide new value for the purposes of cl 2(1)(b)(i)(C) of Schedule 7 of the Act, the maximum priority Heartland could claim over the preferential creditors would be the $11,158.09.

Submissions for Heartland

[117] Ms Wakelin submitted that, because of the absolute assignment of the debts, the liquidators had no authority to deal with the debts other than as Heartland's collection agents. They had no authority to compromise the debts or apply set-offs without Heartland's express agreement.

[118] Ms Wakelin referred to the provisions of cl 11.2.4 and 13.3 of the IFFA. Under cl 11.2.4, Stages warranted and represented that the debtor (for present purposes, Broadspectrum and the shareholder) had not acquired any right of set-off or counterclaim available against Stages in respect of the relevant debt. Under cl 13.3, Stages undertook not to vary, release, or negotiate any debt without Heartland's prior written consent, and to notify Heartland as soon as it became aware of any dispute concerning the payment of a debt owing under a factored invoice. Heartland received no notification of any dispute or right of set-off or counterclaim from either Stages or the liquidators in respect of any of the debts. Nor was Heartland's prior written consent to any variation or release sought at any time by Stages or the liquidators.

[119] The liquidation did not displace Stages' contractual obligations to Heartland, and the liquidators (as agents of Stages) were obliged to observe those contractual obligations.

[120] While Heartland accepts that Broadspectrum may have had an ability to set-off or deduct claims it had against Stages from amounts it owed pursuant to the relevant invoices, it was for Heartland to negotiate with Broadspectrum and agree any set-offs or deductions, not the liquidators.

[121] Section 310 of the Act, which relates to the setting off of mutual credits and mutual debts as between a company in liquidation and a creditor, cannot assist the liquidators. Because of the absolute nature of the assignment of the debts, any moneys owing by Broadspectrum under the invoices were owed to Heartland, not Stages. The mutuality requirement of s 310 is not met.

Discussion and conclusions on Issue (4).

[122] I accept Ms Wakelin's submission that the liquidators' only role in respect of assets which may have remained the subject of a security interest or interests held by Heartland (over which the preferential creditors did not have priority), could have been as collection agent for Heartland. Beyond that role, the liquidators could have had no rights to deal with such assets. That said, the conclusions I have reached above mean that the liquidators always had the statutory right under cl 2(1)(b)(i) and (ii) to collect the $20,000 from the shareholder for the benefit of the preferential creditors (and to resist Heartland's claims that they were not entitled to do so). Conversely, the preferential creditors have never had any priority under cl 2(1)(b)(i) over the amount realised from the invoice for $105,372.20 issued by the liquidators in November 2016, and the liquidators have never had any rights to act in respect of that asset other than as collection agent for Heartland.

[123] The Broadspectrum claims which the liquidators agreed to set off against Stages' claims under the four invoices had no apparent relationship with Stages' claim for $20,000 against its shareholder, and to the extent that a set-off was agreed it must all have been against the amounts invoiced by Stages and the liquidators to Broadspectrum. The result must accordingly be that $20,000 out of the Fund, less any

costs, is available to be applied towards the preferential creditor claims of the employees of Stages and the Inland Revenue, pursuant to Schedule 7 of the Act. As the preferential creditors have no priority claim to it as an "account receivable", such part of the $105,372.20 invoiced by the liquidators to Broadspectrum in November 2016 as is represented in the Fund is now available for distribution, subject to any costs deduction that might be appropriate, to Heartland.

[124] Beyond that I do not consider it appropriate to give directions on Issue (4) before I have received counsel's further submissions on Issue (3)(iv).

[125] I add that in providing the directions sought by the liquidators it is neither necessary nor appropriate for me to address directly any claim Heartland might consider it has against the liquidators personally for wrongfully dealing with assets that might be subject to Heartland's securities (including by settling with Broadspectrum without Heartland's knowledge or approval). That includes the issue of when the liquidators' authority to act as Heartland's collection agent in respect of assets in which Heartland had a (prior) security interest may have ceased. Any such issues would need to be raised by Heartland in a separate proceeding against the liquidators.

Issue (5) — Can the liquidators deduct their fees (other than reasonable salvage costs incurred in recovering the accounts receivable) from the Fund?

[126] In my view this is an issue on which the parties should have the opportunity to make further submissions in the light of the rulings I have made in this interim judgment.

Result

[127] I give the following directions under s 284(1) of the Act:

(1) On Issue (1), directions in accordance with paragraph [70] of this judgment.

(2) On Issue (2), directions as follows:

(i) The amount of $20,000 owed to Stages by its shareholder, and the amounts of the three invoices issued by Stages before the liquidation to Broadspectrum which were unpaid at the date of the liquidation, were all "accounts receivable" of Stages for the purposes of cl 2(1)(b)(i) of Schedule 7 of the Act.

(ii) The work in progress at liquidation date later invoiced by the liquidators to Broadspectrum for $105,372.20 was and is not an "account receivable" (or the proceeds of realisation thereof) for the purposes of cl 2(1)(b)(i), and that clause did not confer any priority on the preferential creditors in respect of it.

(3) On Issues (3)(i), (ii) and (iii), directions in accordance with (respectively) paragraphs [81], [82] and [90] of this judgment.

(4) On Issue (3)(iv), I direct in accordance with paragraph [99] of this judgment that, for the purposes of cl 2(1)(b)(i)(C) of Schedule 7 of the Act, Heartland did not provide "new value" to acquire the account receivable comprised in the $20,000 owing to Stages by its shareholder. In respect of other matters arising under Issue (3)(iv), I direct that counsel are to file further submissions directed to the issue identified at paragraph [102] of this judgment. Heartland is to provide its written submissions within 15 working days of the date of this judgment, and the liquidators are to provide their written submissions within 10 working days after Heartland's written submissions have been served on them.

(5) On Issue (3)(v), I make directions in accordance with paragraphs [110] and [111] of this judgment.

(6) On Issue (4), I make directions in accordance with paragraphs [122] and [123] of this judgment.

(7) On Issue (5), I direct that, within 15 working days of the date of this judgment, Heartland is to file and serve further written submissions on what amounts (if any) should be deducted from each component of the Fund for the liquidators' fees and/or for the parties' costs of the proceeding. The liquidators are to file and serve their written submissions in reply, within 10 working days of service on them of Heartland's submissions.

(8) If and to the extent there remains an issue over the parties' entitlements to interest on the Fund, counsel are to address that issue in the written submissions to be filed under (7) above.

(9) Leave is reserved to the parties to apply by memorandum, within the same periods referred to in (7) above, for any supplementary directions that may be required.

Associate Judge Smith